No. 8662

In the
United States
Circuit Court of Appeals
for the Ninth Circuit

MARGARET D. KLEINSCHMIDT, as Administratrix of the Estate of Walter Granger Kleinschmidt, Deceased,
Appellant,

vs.

ERNEST U. SCHROETER, as Trustee in Bankruptcy of the Estate of B. F. Baum, a Bankrupt,
Appellee.

Petition for Rehearing

RUPERT B. TURNBULL,
Title Insurance Building,
433 South Spring Street,
Los Angeles, California,
Solicitor for Appellee.

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CERTIFICATE OF GOOD FAITH BY COUNSEL PRESENTING PETITION FOR REHEARING

UNITED STATES OF AMERICA)
STATE OF CALIFORNIA) SS
COUNTY OF LOS ANGELES)

I, Rupert B. Turnbull, the solicitor for the appellee, Ernest U. Schroeter, Trustee in Bankruptcy, hereby certify that the within petition for rehearing presented and filed on behalf of the appellee, trustee in bankruptcy, in my judgment is well founded in fact and in law; that said petition for rehearing is not interposed for delay. That said petition is filed for the purpose of calling attention of this court to reasons why the decision in this matter is not correct.

RUPERT B. TURNBULL,

Solicitor for Appellee, Ernest U. Schroeter, Trustee in Bankruptcy of the Estate of Benjamin F. Baum.

In the
United States
Circuit Court of Appeals
for the Ninth Circuit

MARGARET D. KLEINSCHMIDT, as Administratrix of the Estate of Walter Granger Kleinschmidt, Deceased, *Appellant,* vs. ERNEST U. SCHROETER, as Trustee in Bankruptcy of the Estate of B. F. Baum, a Bankrupt, *Appellee.*	No. 8662

Petition for Rehearing

To the Honorable Chief Justice and the Associate Justices of the United States Circuit Court of Appeals for the Ninth Circuit, and to Justices Garrecht, Mathews and Haney, Circuit Judges Thereof:

The appellee files this his petition for a rehearing for the purpose of calling to the attention of this court the several ways in which he sincerely believes this court has reached an erroneous decision, to-wit, in its

decree severely modifying the original judgment obtained in the lower court in favor of this appellee, and as his grounds and reasons therefor hereby states:

GROUNDS FOR THIS PETITION

I.

That from a reading of the opinion of this court deciding this matter it appears that the court has not at all considered the allegations of fraud, the findings of fraud by the trial court, the conclusions of fraud found by the trial court, as the basis of the action and the recovery as decreed by the trial court.

II.

That this court has not considered that a person hopelessly insolvent, owing in excess of $90,000, and with property other than that fraudulently conveyed worth less than $1,000, cannot make an agreement, express or implied, to abandon his interest in property, even though it be a contract to purchase, under the terms of which agreement to abandon, either express or implied, it is arranged that he is to have the return of his interest in the contract after he is discharged from bankruptcy, and thus deprive his creditors of an asset which they might have saved.

III.

That the trustee in bankruptcy becomes the owner of property not only which the bankrupt had at the

date of adjudication but which, according to the language of Section 70-A of the Bankruptcy Act includes

> "property transferred by him in fraud of his creditors"

and

> "property which prior to the filing of the petition he could by any means have transferred."

IV.

That the court has not taken into consideration that the fraudulent abandonment of the executory contract to purchase the Camp Rock Mine and the agreement between the parties to abandon it temporarily, occurred within the inhibited four months' period, prior to bankruptcy.

V.

That the court has overlooked and not taken into consideration the fact that fraud is always a question of fact and that the facts have been found by the lower court. That the trial court saw and observed the parties and chose to disbelieve the witness Baum, whose testimony this court now uses as a basis for the reversal of the trial court.

ARGUMENT

At the time set for oral argument counsel for this appellee was unable, by reason of previous engagements in the District Court, to appear personally and

answer the oral arguments of the appellant, and feeling the matter had been properly covered by briefs, submitted the matter upon the briefs on file. Upon the reading of the learned opinion of this court it is obvious to the appellee and his counsel that the court has entirely overlooked and not considered the situation which was presented in fact and in law to the lower court. The opinion rendered by this court is logical and upon the premises assumed, the reasoning leads incontrovertibly to the conclusion reached by this court in its opinion modifying the decree of the lower court. Our difference of opinion is upon the premises, not the logic, involved. This court assumes that Benjamin F. Baum was an honest man, that his testimony was true and that the court should have believed him, and this court obviously does believe his testimony. The record shows that Benjamin F. Baum, the bankrupt, owed in excess of $90,000 and had no assets other than property which produced less than $1,000 in the bankruptcy court. The Findings show that Benjamin F. Baum, the bankrupt, knowing this, permitted the default and also assigned the only other asset he had to his partner, Kleinschmidt, within 60 days before his voluntary bankruptcy. That he received his interest in that contract back from his partner Kleinschmidt four days after he was granted a discharge in bankruptcy and sold the property for $50,000, all cash. This court assumes that those two transactions were honest, that they were fair. This court indulges in that assumption as a premise for its logical reasoning to the conclusion

now reached. This court indulges in that assumption of fair dealing, honesty of purpose, notwithstanding the finding of the lower court that the rights of Baum in the joint adventure contract were found to have been given by Baum to Kleinschmidt as a sham and for the purpose of concealing them from the creditors of Baum until he should have obtained his discharge. This was a finding of fact which is contained in the transcript of record, page 39, and reads:

> "Benjamin F. Baum scheduled debts in excess of $90,000.00, and that in contemplation of said bankruptcy proceedings, which were voluntary on the part of Benjamin F. Baum, he did, on the 12th day of September, 1931, and less than sixty days prior to the filing of his bankruptcy on November 6, 1931, and while he was indebted to creditors in a sum in excess of $90,000.00, he, the said Benjamin F. Baum, entered into an agreement with Walter Granger Kleinschmidt, who was then a person jointly interested with him in the said mining property hereinbefore described, the Camp Rock Mining Property.
>
> "That at said time it was agreed by and between the said Benjamin F. Baum and said Walter Granger Kleinschmidt that Benjamin F. Baum should assign his interest in and to said mining property and his, Benjamin F. Baum's, contractual rights therein and thereto, and convey the same to Walter Granger Kleinschmidt. That Walter Granger Kleinschmidt agreed that he would hold the same as the property of Benjamin F. Baum, to

and until such time as Benjamin F. Baum should be free of entanglements and obligations of his, the said Benjamin F. Baum's, creditors. That said Walter Granger Kleinschmidt then and there agreed to reconvey said property at a date in the future and at a time when said Benjamin F. Baum should request the same, and at a time when and after Benjamin F. Baum should be free of and from the obligations of his, Benjamin F. Baum's creditors. That on September 12, 1931, Benjamin F. Baum made and delivered to Walter Granger Kleinschmidt an instrument purporting to assign to Kleinschmidt his interest in the mining property hereinbefore described.

"The court finds that thereafter proceedings for the administration of Benjamin F. Baum as a bankrupt were had, that Benjamin F. Baum did not disclose to the trustee in bankruptcy in his estate, to-wit, Ernest U. Schroeter, nor to the Referee in Bankruptcy before whom the bankruptcy proceeding was pending, nor to the creditors of Benjamin F. Baum, that Benjamin F. Baum had an interest or had had any interest in and to the said Camp Rock mining property hereinbefore described, or any contractual or other interest therein or thereto."

The lower court then proceeds to find, and does find, that THAT VERY AGREEMENT WAS CONSUMMATED and that four days after the discharge of Baum he got a reconveyance from his partner Kleinschmidt. The trial court had before it Benjamin

Baum; he observed the utter impeachment of the man on the witness stand, he observed his demeanor and he found that the story which he told was untrue. Surely this court cannot be so naive as to believe that a man owing $90,000 would take his one substantial asset, allow it to be forfeited a few days before his bankruptcy, get it back from his partner four days after his discharge in bankruptcy without consideration and sell it for a profit of $21,000, and then believe that the conveyances were innocent. This court in its opinion disposes of this fraud matter by saying in its opinion:

> "Kleinschmidt, on November 15, 1932, assigned to Baum a one-half interest in his profits from the sale of Camp Rock Mine. This assignment was of no interest or concern to appellee."

The trial court found it was the consummation of the agreement to secrete.

It is no answer to say that the transfer of the rights of Baum were by operation of law rather than by his voluntary written assignment. That is merely calling the acts of Baum names. The fact is obvious, and was so found by the trial court, that the alleged default and the transfer to complete it made by Baum shortly before bankruptcy was a part of a scheme to take that Camp Rock property beyond the reach of Baum's creditors. That it was kept beyond the reach of Baum's creditors with the knowledge on the part of Kleinschmidt that Baum had gone into bankruptcy and it was not given back to Baum until four days after he

was discharged. The record shows conclusively that there was no legal consideration for the transfer back to him four days after his discharge. There is presented in this case in fact a crude attempt by two partners to save one partner's interest until after he should obtain his discharge in bankruptcy. Under the findings of the trial court the parties are not permitted to do this because the court found there was a fraud in fact and by the acts of the parties. If the present decision of this court modifying that decree is to stand, then the very fraud of transfer and concealment and retransfer back into the hands of the guilty party is accomplished and upheld. Every fraud may be explained away upon logical grounds if we take as the premise the story of the persons who are parties to the fraud.

Can a debtor, hopelessly insolvent, agree, expressly or impliedly, to abandon to his partner temporarily or for the term of the debtor's bankruptcy, the interest of the bankrupt in a valuable contract or any valuable property, conceal the facts from the bankruptcy court, the trustee and the creditors, and obtain the return of his interest four days after he is discharged and retain it with impunity? This court has given the answer to this query in the affirmative. This court has absolutely ignored the finding of fact made by the trial court based upon the facts; based upon the court's observation of the parties before him, their demeanor on the stand, and the relation of the facts one to the other. That finding is Finding II in the Findings of Fact found in the Transcript of Record in this case,

pages 39 and 40. This court has taken the testimony of Mr. Baum, a witness who was shown to have acted dishonestly in his bankruptcy proceedings and in relation to his creditors and with respect to the very testimony he gave in this proceeding, and has taken that testimony which the trial court did not believe, and this court has used it as the basis of fact to reverse the trial court. We respectfully challenge the right of this court to disregard a finding of fact and the logical conclusion of law following therefrom. Section 1574 of the Civil Code of California reads:

> "Section 1574. Actual fraud a question of fact. Actual fraud is always a question of fact."

Section 1, Subdivision 25, of the Bankruptcy Act reads:

> " 'Transfer' shall include the sale *and every other and different mode of disposing of or parting with property.* . . ."

Section 70-A of the Bankruptcy Act provides that the trustee of the estate of a bankrupt shall be vested by operation of law with

> "property transferred by him in fraud of creditors, property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him."

Prior to bankruptcy and within the four months' period defined in the Bankruptcy Act, Baum did have a substantial interest in his contract for the purchase

of the Camp Rock Mine. Within that four months period prior to bankruptcy he could not have given that property away, he could not have transferred it, and of course he could not have entered into an agreement with the person with whom he was jointly purchasing the property, Mr. Kleinschmidt, to forfeit his rights in it subject to its being given back to him four days after he was discharged in bankruptcy.

The learned opinion in this matter by this court makes no mention in any place, with the element of fraud, with the secret agreement between the parties, either as alleged in the complaint or as found by the court in its Findings of Fact and Conclusions of Law. This court in its opinion dismisses any such theory, proof, findings and conclusions of the trial court by the simple sentence,

> "Kleinschmidt on November 15, 1932, assigned to Baum a one-half interest in his profits from the sale of Camp Rock Mine. This assignment was of no interest or concern to appellee."

THE LAW

12 Cal. Jur. 1059, Sec. 97:

> ". . . The burden shifts to the transferee to establish that the transaction was in good faith and not fraudulent whenever the evidence is sufficient to establish a *prima facie* case of fraud, *or the circumstances are such that an inference or statutory presumption of fraud arises.*"

McKinney, Trustee in Bankruptcy, v. Wright, 105 Cal. App. 401:

Syl. 3. "In such action, the husband having rendered himself bankrupt by the conveyance to his wife, *the intent will be inferred* that the transfer was made for the purpose of rendering himself insolvent."

Judson v. Lyford, 84 Cal. 505 (p. 508):

"Nor is it necessary that the grantor should have had any malice against the creditor, or any evil intent to injure him or any actual intent to do a wrong. It is immaterial whether, as a matter of fact, he supposed that he had a perfect right to conceal his property from his creditors. *Concealment of property from one's creditor is what the law forbids, and the intent so to conceal it is considered fraud;* and it is sufficient so to plead it."

Benson v. Harriman, 55 Cal. App. 483:

Syl. 3. "Where a transfer renders one insolvent his insolvency is contemplated by the very act of making the transfer."

Syl. 4. "Intent is immaterial where the transfer is made without consideration and in contemplation of insolvency."

Syl. 7. *"The existence of an indebtedness at the time of a voluntary conveyance creates at least a prima facie presumption of fraud."*

12 Cal. Jur. 1018, Sec. 60:

"Prior to the enactment of section 3442 of the Civil Code in 1895, insolvency itself was not suffi-

cient to make a voluntary conveyance void as to creditors. Insolvency was, however, strongly persuasive of an intent to defraud, and while not conclusive as a matter of law, was frequently of sufficient strength, coupled with other facts, to justify a finding of the existence of fraudulent intent.

The amendment of 1895 completely changed this rule. By express provision, a voluntary conveyance made by an insolvent, or by one in contemplation of insolvency, is now *conclusively presumed to be fraudulent as to existing creditors.* The insolvency of the voluntary grantor is conclusive of fraudulent intent, and *no other facts can control, influence or overcome this presumption. The question of an actual intent is immaterial.*"

12 Cal. Jur. 981, Sec. 23:

"By the provision of the national bankruptcy act, the trustee in bankruptcy *may avoid any transfer* by the bankrupt *which any creditor* might have avoided, and may therefore maintain an action to set aside property conveyed in fraud of such creditors."

12 Cal. Jur. 1017, Sec. 59:

"The intent to defraud creditors which is necessary to avoid a voluntary conveyance is a question of fact and not a question of law, *except where the transfer is made while insolvent or in contemplation of insolvency;* and no acts are conclusive as a matter of law that such intent exists, though they may be sufficient to justify an inference of its existence. Thus, *an inference of fraud may*

arise from the absence of a valuable consideration when coupled with other suggestive circumstances, such as the fact that the grantor is heavily indebted and had no other property out of which his obligations can be satisfied. . . . Similarly, a voluntary conveyance is evidence of fraud when made by the debtor to prevent his property from being attached, or when made after service upon him of an order to appear and testify as to his property."

Daniel v. Sisnero, 109 Cal. App. 8:

Syl. 4. "Where said debtor testified that he received no consideration for the deed to his father, and that the conveyance rendered him insolvent, these facts, with the fact, properly found by the trial court, that the property belonged to the debtor and not to his father, sufficiently showed fraud under section 3442 of the Civil Code, and there was no error in finding that the conveyance was made for the purpose of defrauding plaintiff creditor, and to prevent him from collecting his judgment against the debtor."

Vogel v. Sheridan, 4 Cal. App. (2d) 298—(hearing by Supreme Court denied):

Syl. 3. "Both sections 3439 and *3442* of the Civil Code should be liberally construed to effect their purpose to prevent debtors from placing property which legitimately should be available for the satisfaction of demands of creditors beyond their reach; and it is only in actions maintained under the proviso in said section 3442 that the insolvency of the transferor becomes of controlling

importance, and *in such actions the question of actual intent becomes immaterial.*"

The court said (p. 305):

"It is only in actions maintained under the proviso in section 3442 that the insolvency of the transferor becomes of controlling importance and in such actions, the question of actual intent becomes immaterial. The distinction is pointed out in Hanscome-James-Winship v. Ainger, 71 Cal. App. 735 and Allee v. Shay, 92 Cal. App. 749. It has been stated that *both sections should be liberally construed to effect their purpose which 'undoubtedly is to prevent debtors from placing property which legitimately should be available for the satisfaction of demands of creditors beyond their reach.'* (Borgfeldt v. Curry, 25 Cal. App. 624, 626)."

Southwick v. Moore, 61 Cal. App. 585. (Hearing denied by Supreme Court):

Syl. 2. "Where a husband made a conveyance of the only property he owned to his wife and she withheld the deed from record, the exercise of acts of ownership by the husband subsequent to the execution of the deed with the knowledge of the wife is strongly suggestive of fraudulent intent as to creditors."

The court said (p. 590):

"We pass to a consideration of the evidence as supporting the finding that the deed was made to hinder, delay, and defraud creditors. If there could be any dispute as to Moore's insolvency be-

fore the deed was executed there certainly can be no shadow of doubt that by making the conveyance of the only property he owned he became insolvent and that the transfer was made 'in contemplation of insolvency.' . . . Such a transfer is void as to existing creditors. (Sec. 3442, Civ. Code). . . . The continued control of the property after the conveyance is further evidence of fraudulent intent. . . .

As said in Schell v. Gamble, 153 Cal. 448, the burden of proof is upon the creditor to establish the fact of the fraudulent intention of the grantor; that burden is, however, sustained where a *prima facie* case is made out. As we have shown in the instant case, the creditor added other evidence to a *prima facie* showing. *Of course, the evidence was circumstantial, but that is usual in such cases.* It is also true that the record contains other testimony, especially that of the appellant, tending to contradict the respondent's proof. It has not been necessary to give this extended consideration, since *it is not the province of an appellate court to weigh and contrast the evidence.*"

12 Cal. Jur., 1059, Sec. 98:

"When the question of fraud is involved great latitude is allowed in the admission of evidence. *Positive proof of fraud can be seldom obtained, for fraud itself is always concealed. It is usually disclosed only by the circumstances of the transaction and its irregularities,* or from the interests of the parties coupled with the injury to innocent persons, *rather than by direct evidence.* So in attacking a conveyance for fraud as to him, a credi-

tor, in proof of the fraudulent intent of the debtor, may offer in evidence *any fact or circumstance which will have a tendency to establish such intent,* such as evidence of the relation existing between the parties and the nature of the transaction, the contemporaneous and *subsequent conduct* of the parties and the grantor's declarations before the conveyance, the existence of the obligation prior to insolvency, want of consideration, and a threat of legal proceedings made against the vendor. *Declarations* of the parties, while admissible under certain circumstances, *are not of as great a probative value as the facts of the transaction themselves.*"

CONCLUSION

We respectfully submit that if the court will consider the findings of the trial court and the evidence in the record which supports them and the circumstances which support them, it will arrive at the same conclusion as did the trial court. If this court continues to assume that Benjamin Baum told the truth, if it continues to take the testimony as entirely true of this discredited party and witness, it will give its stamp of approval to a surreptitious arrangement between the parties Kleinschmidt and Baum which resulted in the loss of the only valuable asset of the bankrupt and it will permit the accomplishment of an actual fraud. We are confident that if the court will consider the decision of the trial court in the light of the facts and that there was a fraud and that the circumstances and evidence show an agreement between the parties to permit a

default, conceal the property until after Baum received his discharge and then to have it reconveyed to him, this court will correct an injustice which would have occurred had the original opinion of this court been permitted to stand.

Respectfully and confidently submitted,

RUPERT B. TURNBULL,

Solicitor for Appellee Ernest U. Schroeter, Trustee in Bankruptcy of the Estate of B. F. Baum.